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ABSTRACT

This document consists of 19 exhibits that outline information on contractual risk transfers. Topics include the following: types of risk-treatment techniques; an overview of the process for using indemnity and insurance clauses; the rationale for contractual risk transfer; residual risks in contractual transfer; the rationale for and types of indemnity clauses; points to look for in indemnity agreements; types of insurance to require; a risk-management/insurance checklist; liability insurance clause--PRIMA; alternative insurance clauses; the PRIMA general-liability endorsement; an alternative commercial general-liability endorsement; the property insurance standard clause; certificate of insurance; a protection scale; the process for dealing with non-compliance; guidelines for contract insurance provisions; and nine points to know about accepting certificates of insurance. (LMI)

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ADVANCED RISK MANAGEMENT TECHNIQUES, INC.

ED 366 073

CONTRACTUAL RISK TRANSFER
Passing the Hot Potato Without Getting Burned

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Presented to: ***ASBO International***
October 30, 1993
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LIST OF EXHIBITS

1 Risk Treatment Techniques

2 Overview of Process for Using Indemnity and Insurance Clauses

3 Why Transfer Risks by Contract?

4 Inherent Risks in Contractual Transfer

5 Why Use Insurance and Indemnity Clauses?

6 Types of Indemnity Clauses

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8 Types of Insurance to Require

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10 Liability Insurance Clause - PRIMA

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17 Dealing with Non-Compliance

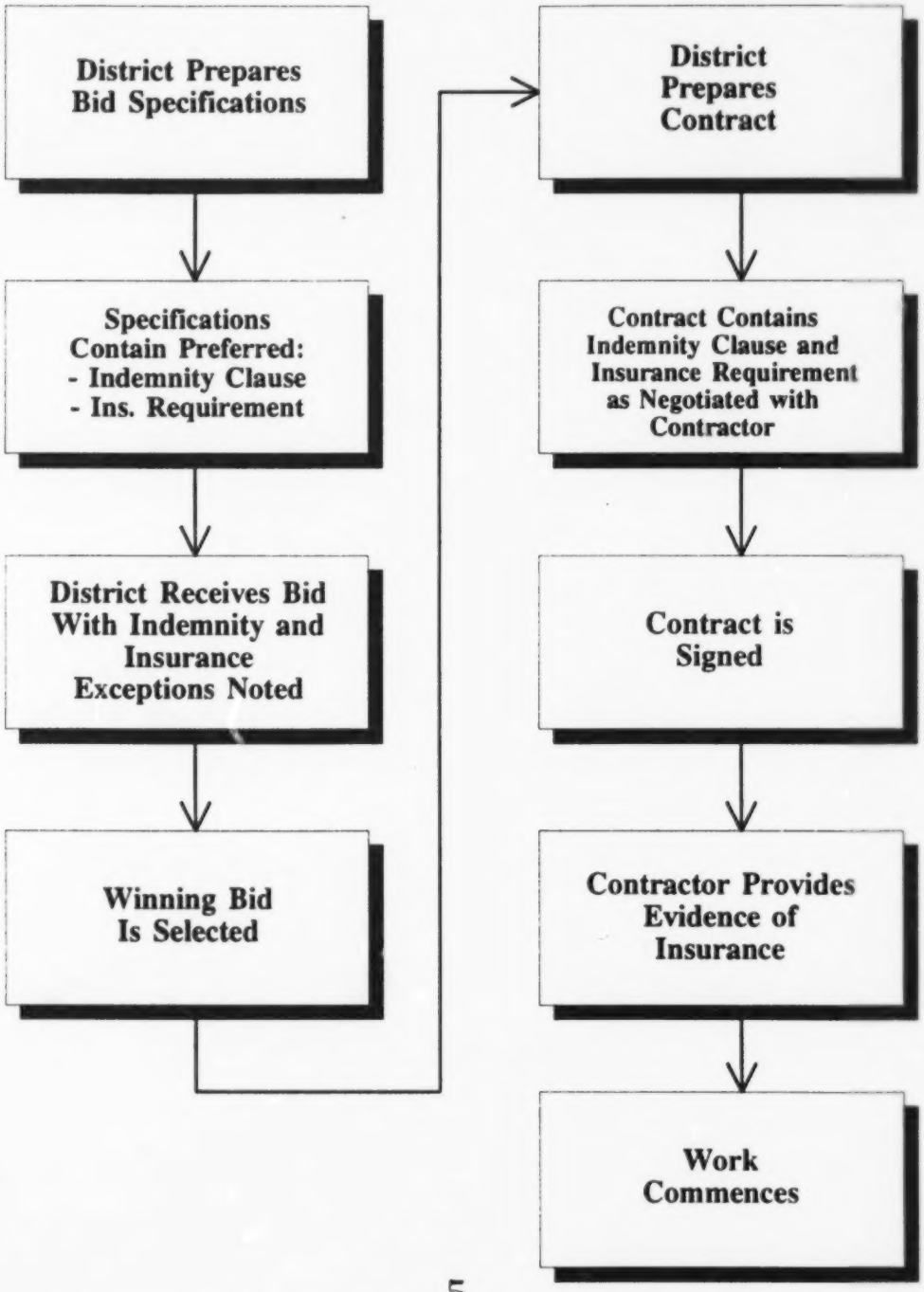
18 Guidelines for Contract Insurance Provisions

19 Nine Points to Know about Accepting Certificates of Insurance

References

RISK TREATMENT TECHNIQUES

OVERVIEW OF PROCESS FOR USING INDEMNITY AND INSURANCE CLAUSES


District Prepares Bid Specifications
Specifications Contain Preferred:
- Indemnity Clause
- Ins. Requirement
District Receives Bid With Indemnity and Insurance Exceptions Noted
Winning Bid Is Selected
District Prepares Contract
Contract Contains Indemnity Clause and Insurance Requirement as Negotiated with Contractor
Contract is Signed
Contractor Provides Evidence of Insurance
Work Commences

WHY TRANSFER RISKS BY CONTRACT?

1. **Required by law.**

2. **Transferee can handle better:**

   a. **Experience.**

   b. **Financial capacity.**

   c. **Position to control.**

3. **Protect the district's insurance or self-insurance program.**

RESIDUAL RISKS IN CONTRACTUAL TRANSFER

1. **Incompetent contractor.**
2. **Public nuisance from the nature of the project.**
3. **Supervisory acts resulting in loss.**
4. **Contractor does not buy coverage you intended.**
5. **Breach of insurance policy by contractor.**
6. **Policy cancelled.**
7. **Other insurance clause.**
8. **Contractor employee claim.**
9. **Inadequate limits.**
10. **Policy exclusions.**
11. **Contractor failure.**
12. **Insurance company failure.**

WHY USE INSURANCE AND INDEMNITY CLAUSES?

1. **Indemnity Clause**

   - **States who is responsible for injury or damage arising out of the work performed.**
   - **Usually does not contain a dollar limit.**
   - **Usually is not limited in the types of injury or damage to which it applies.**
   - **Provides an avenue for recovery if contractor's insurance is invalid.**
   - **Indemnitee - Person or organization held harmless (usually your district).**
   - **Indemnitor - Person or organization (usually the contractor) agreeing to indemnify the other party to the contract (the indemnitee).**

2. **Insurance Requirement**

   - **Specifies the types and limits of insurance contractor must buy.**
   - **Helps ensure that contractor has funds available to pay liability assumed under indemnity clause.**
   - **Can give the district some specific rights under contractor's policies.**

3. **Points to Consider**

   - **The legal enforceability of the transfer.**
   - **The abilities of the parties to manage risk.**
   - **The price of the transfer.**

TYPES OF INDEMNITY CLAUSES

1. ***Limited Form.*** **Requires contractor to be responsible for its own negligence.**

   Sample Clause: "Contractor agrees to hold harmless and indemnify District for liability arising out of the negligent activities of Contractor.

2. ***Intermediate Form.*** **Requires contractor to be responsible for its own negligence and the joint negligence of the Contractor and the District.**

   Sample Clause: "Contractor agrees to hold harmless and indemnify the District for all liability arising out of the project, except that arising out of the sole negligence of the District."

3. ***Broad Form.*** **Requires contractor to be responsible for all liability arising out of the project (including the sole negligence of the District).**

   Sample Clause: "Contractor agrees to hold harmless and indemnify District for all liability arising out of the project."

POINTS TO LOOK FOR IN INDEMNITY AGREEMENTS

The indemnity agreement should apply to:

1. **Acts of the:**

   - **Contractor.**
   - **Contractor's employees and agents.**
   - **Contractor's subcontractors.**

2. **The sole negligence of the contractor and the joint negligence of the contractor and the district.**

3. **All types of injury or damage arising out of the project, not just bodily injury and property damage.**

4. **Damages or injury to:**

   - **Contractor's employees and agents.**
   - **Contractor's property.**
   - **Third parties.**

5. **Defense of the District.**

TYPES OF INSURANCE TO REQUIRE

Type of Contract	Comm'l General Liab.	Business Auto Liab.	Prof. Liab.	Aircraft and Airport Liab.	Fire and Extended Coverage or All Risk	Workers' Compen-sation
Construction Contract* (new construction)	✓	✓			●	✓
Lease (tenant of entire building or ground lease with building reverting to district)	✓				✓	
Professional Service Contract (architects, engineers, doctors, etc.)	✓	●	✓			✓
Airline, FBO or Aircraft Transport		●		✓		✓
Transportation Contractor or where contract requires substantial use of automobiles	✓	✓			●	✓

✓ = Coverage normally required in contract situation.

● = Coverage often (but not always) required in contract situation.

* = For construction projects exceeding $100 million or more in construction costs, District should evaluate whether it should arrange commercial general liability and workers' compensation for all contractors and subcontractors on-site. This is called an owner controlled or wrap-up program.

RISK MANAGEMENT/INSURANCE CHECKLIST

Author of Contract	Telephone Number
Contract Description	Amount
Bureau/Division Responsible	
Location of Project (street address or address range)	

Please indicate which of the following best describes the major type of contract:

✓	Construction	✓	Repair and Maintenance	✓	Engineering Professional
	Buildings and Structures		Buildings		Environmental Study/Management
	Installation of Facilities		Equipment		Inspection
	Electrical		Piers/Docks		Construction Manager
	Plumbing		Vehicles		Design
	Heat/Ventilating and Air Conditioning				Topographical/Utility Survey
		✓	**Other Services**		
✓	**Other Professional**		Cleaning	✓	**Marine Services**
	Expert/Study Only		Inspection/Assessment		Dredging
	Medical Service		Armored Car		Towing of Vessels
	Legal Service		Collection Agency		Marine Survey
			Gas Detection		Maintenance and/or Repair of Vessels
			Computer		

RISK MANAGEMENT/INSURANCE CHECKLIST

Please indicate whether each of the following applies and enclose sections of contract referring to these special exposures.

Yes (✓)	No (✓)	Hazard	Contract	
			Section	Page
		Operations in area with possible mercury, PCB, HZS, asbestos, methane, gas or other toxic/explosive or hazardous materials		
		Excavation or construction within 50 feet of any rail facility, lake, stream, pond or other waterway		
		Excavation in public streets		
		Blasting/utilization or storage of any explosives		
		Utility support and protection		
		Access to any district non-owned property or property not under district control		
		Use of any watercraft or marine equipment or of any aircraft		
		Provision of vehicle, watercraft or aircraft		
		Tunneling		
		Pile driving		
		Use of any district tools and equipment by contractor		

LIABILITY INSURANCE CLAUSE - PRIMA

Contractor shall procure and maintain for the duration of the contract insurance against claims for injuries to persons or damages to property which may arise from or in connection with the performance of the work hereunder by the Contractor, his agents, representatives, employees or subcontractors.

A. MINIMUM SCOPE OF INSURANCE

Coverage shall be at least as broad as:

1. **Insurance Services Office Commercial General Liability coverage ("occurrence" form CG 0001, Ed. 11/88)**

2. **Insurance Services Office form number CA 0001 (Ed. 6/92) covering Automobile Liability, code 1 "any auto."**

3. **Workers' Compensation insurance as required by the Labor Code of the State of _____ and Employers Liability insurance.**

B. MINIMUM LIMITS OF INSURANCE

Contractor shall maintain limits no less than:

1. **Commercial General Liability: $1,000,000 combined single limit per occurrence for bodily injury, personal injury and property damage. The general aggregate limit shall apply separately to this project/location or the general aggregate shall be twice the required occurrence limit.**

2. **Automobile Liability: $1,000,000 combined single limit per accident for bodily injury and property damage.**

3. **Workers' Compensation and Employers Liability: Workers' compensation limits as required by the Labor Code of the State of _____ and Employers Liability limits of $1,000,000 per accident.**

LIABILITY INSURANCE CLAUSE - PRIMA

C. DEDUCTIBLES AND SELF-INSURED RETENTIONS

Any deductibles or self-insured retentions must be declared to and approved by the Agency. At the option of the Agency, either: the insurer shall reduce or eliminate such deductibles or self-insured retentions as respects the Agency, its officers, officials, employees and volunteers; or the Contractor shall procure a bond guaranteeing payment of losses and related investigations, claim administration and defense expenses.

D. OTHER INSURANCE PROVISIONS

The policies are to contain, or be endorsed to contain, the following provisions:

1. **Commercial General Liability and Automobile Liability Coverages**

   a. **The Agency, its officers, employees and volunteers are to be covered as insureds as respects: liability arising out of activities performed by or on behalf of the Contractor including the insured's general supervision of the Contractor; products and completed operations of the Contractor; premises owned, occupied or used by the Contractor, or automobiles owned, leased, hired or borrowed by the Contractor. The coverage shall contain no special limitations on the scope of protection afforded to the Agency, its officers, officials, employees or volunteers.**

   b. **The Contractor's insurance coverage shall be primary insurance as respects the Agency, its officers, officials, employees and volunteers. Any insurance or self-insurance maintained by the Agency, its officers, officials, employees or volunteers shall be excess of the Contractor's insurance and shall not contribute to it.**

   c. **Any failure to comply with reporting provisions of the policies shall not affect coverage provided to the Agency, its officers, officials, employees or volunteers.**

   d. **The Contractor's insurance shall apply separately to each insured against whom claim is made or suit is brought, except with respect to the limits of the insurer's liability.**

LIABILITY INSURANCE CLAUSE - PRIMA

2. **Workers' Compensation and Employers Liability Coverage**

   The insurer shall agree to waive all rights of subrogation against the District, its officers, officials, employees and volunteers for losses arising from work performed by the Contractor for the Agency.

3. **All Coverages**

   Each insurance policy required by this clause shall be endorsed to state that coverage shall not be suspended, voided, cancelled by either party, reduced in coverage or in limits except after thirty (30) days' prior written notice by certified mail, return receipt requested, has been given to the Agency.

E. ACCEPTABILITY OF INSURERS

Insurance is to be placed with insurers with a Best's rating of no less than A:VII.

F. VERIFICATION OF COVERAGE

Contractor shall furnish the Agency with certificates of insurance and with original endorsements effecting coverage required by this clause. The certificates and endorsements for each insurance policy are to be signed by a person authorized by that insurer to bind coverage on its behalf. The certificates and endorsements are to be on forms provided by the Agency. Where by statute, the Agency's workers' compensation-related forms cannot be used, equivalent forms approved by the Insurance Commissioner are to be substituted. All certificates and endorsements are to be received and approved by the Agency before work commences. The Agency reserves the right to require complete, certified copies of all required insurance policies at any time.

G. SUBCONTRACTORS

Contractor shall include all subcontractors as insureds under its policies or shall furnish separate certificates and endorsements for each subcontractor. All coverages for subcontractors shall be subject to all of the requirements stated herein.

Taken from "Procedure Manual for Contract Insurance Requirements," published by the Public Risk Management Association.

LIABILITY INSURANCE CLAUSE - ALTERNATIVE

3. Insurance

Contractor shall obtain insurance of the types and in the amounts described below.

3.1 Commercial General Liability Insurance. Contractor shall maintain occurrence version commercial general liability insurance or equivalent form with a limit of not less than $1,000,000 each occurrence. If such insurance contains a general aggregate limit, it shall apply separately to this Agreement or be no less than two times the occurrence limit. Such insurance shall:

3.1.1 Include the Agency, its officials, officers and employees as insureds with respect to performance of Services. The coverage shall contain no special limitations on the scope of protection afforded to the above-listed insureds.

3.1.2 Be primary with respect to any insurance or self insurance programs covering the Agency, its officials, officers and employees.

3.2 Business Automobile Liability Insurance. Contractor shall maintain business automobile liability insurance or equivalent form with a limit of not less than $1,000,000 each accident. Such insurance shall include coverage for owned, hired and non-owned automobiles.

LIABILITY INSURANCE CLAUSE - ALTERNATIVE

3.3 Workers' Compensation Insurance. Contractor shall maintain workers' compensation insurance with statutory limits and employers' liability insurance with limits of not less than $1 million each accident.

3.4 Other Insurance Requirements. Contractor shall:

3.4.1 Prior to commencement of Services, furnish the Agency with properly executed certificates of insurance which shall clearly evidence all insurance required in this Section 3 and provide that such insurance shall not be cancelled, allowed to expire or be materially reduced in coverage except on 30 days' prior written notice to the Agency.

3.4.2 Provide certified copies of endorsements and policies if requested by the Agency in lieu of or in addition to certificates of insurance.

3.4.3 Replace certificates, policies and endorsements for any such insurance expiring prior to completion of Services.

3.4.4 Maintain such insurance from the time Services commence until Services are completed.

3.4.5 Place such insurance with insurers licensed to do business in California and having A.M. Best Company ratings of no less than A:VII.

GENERAL LIABILITY ENDORSEMENT - PRIMA

_____ ("the Agency")
_____
_____
Attn:_____

A. POLICY INFORMATION **Endorsement #_____**

1. Insurance Company_____:Policy Number_____
2. Policy Term (From) _____ (To) _____; Endorsement Eff. Date:_____
3. Named Insured_____
4. Address of Named Insured _____
5. Limit of Liability Any One Occurrence/Aggregate $_____/_____

   Commercial General Liability Aggregate (check one):

   Applies "per location/project"
   Is twice the occurrence limit
6. Deductible or Self-Insured Retention (Nil unless otherwise specified): $_____
7. Coverage is equivalent to (check one):

   Comprehensive General Liability form GL0002 (Ed 1/73)
   Commercial General Liability "occurrence" form CG0001
   Commercial General Liability "claims made" form CG0002
8. Bodily Injury and Property Damage Coverage limit is:

   a. "Claims made" _____
   b. "Occurrence" _____

   If claims made, the retroactive date is _____

B. POLICY AMENDMENTS

This endorsement is issued in consideration of the policy premium. Notwithstanding any inconsistent statement in the policy to which this endorsement is attached or any other endorsement attached hereto, it is agreed as follows:

1. **INSURED**. The Agency, its elected or appointed officials, employees and volunteers are included as insureds with regard to damages and defense of claims arising from: (a) activities performed by or on behalf of the Named Insured, (b) products and completed operations of the Named Insured, or (c) premises owned, leased or used by the Named Insured.

GENERAL LIABILITY ENDORSEMENT - PRIMA

2. **CONTRIBUTION NOT REQUIRED**. As respects: (a) work performed by the Named Insured for or on behalf of the Agency; or (b) products sold by the Named Insured to the Agency; or (c) premises leased by the Named Insured from the Agency, the insurance afforded by this policy shall be primary insurance as respects the Agency, its elected or appointed officers, officials, employees or volunteers; or stand in an unbroken chain of coverage excess of the Named Insured's scheduled underlying primary coverage. In either event, any other insurance maintained by the Agency, its elected or appointed officers, officials, employees or volunteers shall be in excess of this insurance and shall not contribute with it.

3. **SCOPE OF COVERAGE**. This policy, if primary, affords coverage at least as broad as:

   (1) Insurance Services Office form number GL 0002 (Ed. 1/73), Comprehensive General Liability Insurance and Insurance Services Office form number GL 0404 Broad Form comprehensive General Liability endorsement; or

   (2) Insurance Services Office Commercial General Liability Coverage, "occurrence" for CG 0001 or "claims made" form CG 0002; or

   (3) If excess, affords coverage which is at least as broad as the primary insurance forms referenced in the preceding sections (1) and (2).

4. **SEVERABILITY OF INTEREST.** The insurance afforded by this policy applies to each insured who is seeking coverage or against whom a claim is made or a suit is brought, except with respects to the Company's limit of liability.

5. **PROVISIONS REGARDING THE INSURED'S DUTIES AFTER ACCIDENT OR LOSS**. Any failure to comply with reporting provisions of the policy shall not affect coverage provided to the Agency, its elected or appointed officers, officials, employees or volunteers.

6. **CANCELLATION NOTICE**. The insurance afforded by this policy shall not be suspended, voided, cancelled, reduced in coverage or in limits except after thirty (30) days' prior written notice by certified mail return receipt requested has been given to the Agency. Such notice shall be addressed as shown in the heading of this endorsement.

C. INCIDENT AND CLAIM REPORTING PROCEDURE

Incidents and claims are to be reported to the insurer at:

Attn: _____
(Title) (Department)

_____
(Company)

_____
(Street Address)

_____
(City) (State) (Zip)

(___) _____
(Telephone Number)

GENERAL LIABILITY ENDORSEMENT - PRIMA

D. SIGNATURE OF INSURER OR AUTHORIZED REPRESENTATIVE OF THE INSURER

I, _____ (print/type name), warrant that I have the authority to bind the below listed insurance company and by my signature hereon do so bind this company.

_____

SIGNATURE OF AUTHORIZED REPRESENTATIVE (original signature required on endorsement furnished to the Agency)

ORGANIZATION:_____ TITLE:_____

ADDRESS:_____ TELEPHONE:( )_____

Taken from "Procedure Manual for Contract Insurance Requirements," published by the Public Risk Management Association.

COMMERCIAL GENERAL LIABILITY ENDORSEMENT - ALTERNATIVE

This endorsement modifies insurance provided under the following:

Commercial General Liability Coverage Part

Policy No. _____

Endorsement Effective Date _____

SCHEDULE

Name of Person or Organization: _____

It is agreed that the policy is amended as follows:

1. **Who is an Insured:** The person or organization shown in the schedule is included as an insured, but only as respects liability arising out of "your work" for that insured by or for you.

2. **This Insurance Applies as Primary:** This insurance is primary as respects any other insurance or a self-insurance program protecting the interests of the person or organization shown in the schedule.

3. **Cancellation or Non-Renewal:** We may cancel or non-renew this coverage part by mailing or delivering to the person or organization shown in the schedule written notice at least 30 days before the effective date of cancellation or non-renewal in coverage.

_____
Insurer

_____
Authorized Agent

PROPERTY INSURANCE STANDARD CLAUSE

Contractor shall purchase a standard form fire and extended coverage property insurance policy to insure:

(Specify facility to be insured)

Insurance will be written in an amount equal to at least 90% of the current replacement cost of the facility. Coverage shall be written on a replacement cost basis. The insurance policy will contain the following clauses:

A. "This insurance shall not be cancelled, limited in scope of coverage or non-renewed until after 30 days' written notice has been given to the District."

B. All rights of subrogation are hereby waived against the District, its officers, employees, and agents.

C. A standard loss payee clause naming the District as loss payee.

Contractor agrees to deposit with the District on or before the effective date of this contract, certificates of insurance necessary to satisfy the District that the insurance provisions of this contract have been complied with and to keep such insurance in effect and the certificates thereof on deposit with the District during the entire term of this contract.

Exhibit 1

ACORD. CERTIFICATE OF INSURANCE

ISSUE DATE (MM/DD/YY)

PRODUCER

THIS CERTIFICATE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE CERTIFICATE HOLDER. THIS CERTIFICA DOES NOT AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY TH POLICIES BELOW.

INSURED

COMPANIES AFFORDING COVERAGE

COMPANY LETTER A

COMPANY LETTER B

COMPANY LETTER C

COMPANY LETTER D

COMPANY LETTER E

COVERAGES

THIS IS TO CERTIFY THAT THE POLICIES OF INSURANCE LISTED BELOW HAVE BEEN ISSUED TO THE INSURED NAMED ABOVE FOR THE POLICY PERIOD INDICATED. NOTWITHSTANDING ANY REQUIREMENT, TERM OR CONDITION OF ANY CONTRACT OR OTHER DOCUMENT WITH RESPECT TO WHICH THIS CERTIFICATE MAY BE ISSUED OR MAY PERTAIN, THE INSURANCE AFFORDED BY THE POLICIES DESCRIBED HEREIN IS SUBJECT TO ALL THE TERMS, EXCLUSIONS AND CONDITIONS OF SUCH POLICIES. LIMITS SHOWN MAY HAVE BEEN REDUCED BY PAID CLAIMS.

CO LTR	TYPE OF INSURANCE	POLICY NUMBER	POLICY EFFECTIVE DATE (MM/DD/YY)	POLICY EXPIRATION DATE (MM/DD/YY)	LIMITS	
	GENERAL LIABILITY				GENERAL AGGREGATE	$
	COMMERCIAL GENERAL LIABILITY				PRODUCTS-COMP/OP AGG	$
	CLAIMS MADE OCCUR				PERSONAL & ADV INJURY	$
	OWNER'S & CONTRACTOR'S PROT				EACH OCCURRENCE	$
					FIRE DAMAGE (Any one fire)	$
					MED EXPENSE (Any one person)	$
	AUTOMOBILE LIABILITY				COMBINED SINGLE LIMIT	$
	ANY AUTO					
	ALL OWNED AUTOS				BODILY INJURY (Per person)	$
	SCHEDULED AUTOS					
	HIRED AUTOS				BODILY INJURY (Per accident)	$
	NON-OWNED AUTOS					
	GARAGE LIABILITY				PROPERTY DAMAGE	$
	EXCESS LIABILITY				EACH OCCURRENCE	$
	UMBRELLA FORM				AGGREGATE	$
	OTHER THAN UMBRELLA FORM					
	WORKER'S COMPENSATION				STATUTORY LIMITS	
	AND				EACH ACCIDENT	$
	EMPLOYERS' LIABILITY				DISEASE—POLICY LIMIT	$
					DISEASE—EACH EMPLOYEE	$
	OTHER					

DESCRIPTION OF OPERATIONS/LOCATIONS/VEHICLES/SPECIAL ITEMS

CERTIFICATE HOLDER

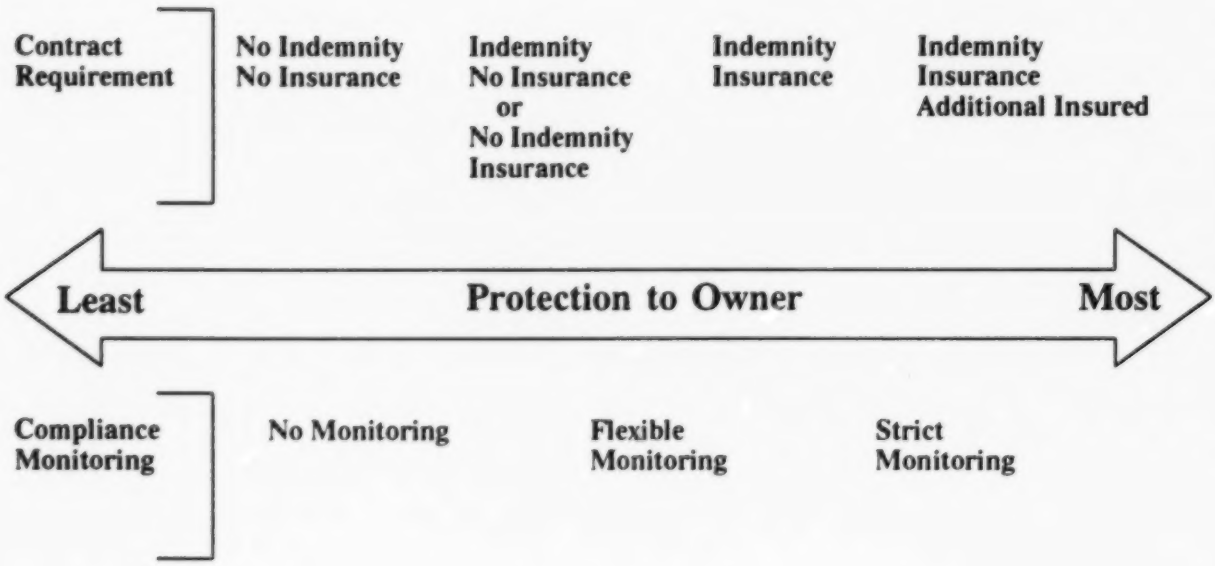
CANCELLATION

SHOULD ANY OF THE ABOVE DESCRIBED POLICIES BE CANCELLED BEFORE THE EXPIRATION DATE THEREOF, THE ISSUING COMPANY WILL ENDEAVOR TO MAIL ____ DAYS WRITTEN NOTICE TO THE CERTIFICATE HOLDER NAMED TO THE LEFT, BUT FAILURE TO MAIL SUCH NOTICE SHALL IMPOSE NO OBLIGATION OR LIABILITY OF ANY KIND UPON THE COMPANY, ITS AGENTS OR REPRESENTATIVES

AUTHORIZED REPRESENTATIVE

BEST COPY AVAILABLE

PROTECTION SCALE



DEALING WITH NON-COMPLIANCE

1. **Learn exactly what the objection is and learn about it early.**

2. **Reduce the required limit (e.g., from $1 million to $500,000).**

3. **Reduce the scope of coverage required.**

4. **Eliminate some special requirements:**

   a. **District insurance is excess.**

   b. **Notice of non-renewal.**

   c. **District as an insured on professional liability insurance.**

5. **Prepare specifications so they allow waiving requirements, if in District's best interest.**

GUIDELINES FOR CONTRACT INSURANCE PROVISIONS

Do . . .

- **Say it precisely and say it once.**
- **Use terms common to current insurance industry usage.**
- **Update language at least annually.**
- **Research all objections to language in advance.**
- **Obtain limits that apply separately to each agency location/contract.**
- **Set up a system to ensure compliance.**
- **Obtain evidence before the job begins.**
- **Consider the cost of compliance.**

Don't . . .

- **Ask for coverage that guarantees every liability assumed in the contract.**
- **Include sensitive environmental work with routine work in same contract.**
- **Tie liability limits to size of contract only.**

NINE POINTS TO KNOW ABOUT ACCEPTING CERTIFICATES OF INSURANCE

- The information on the certificate shows only what coverage applies as of the date on the certificate. It conveys no rights to the certificate holder.

- Many contractors do not provide renewal certificates in a timely fashion as policies expire. That *could* mean a renewal problem where no coverage is in force. A loss is not the way to find out. Requiring contractors to provide a renewal certificate at least 15 days before expiration is a safer method.

- There should be no confusion on what job or operations a certificate applies to. Some of the better ways to do that is to cite a contract number or a job location as a way of tying the insurance to the contracted work. The description block near the bottom of the certificate should not be left empty.

- Certificate notice of cancellation wording that states the insurer will "endeavor to" provide notice to the certificate holder only means the insurer will *try* to send notice. There is no obligation that the insurer send notice, even if the certificate's "endeavor to" wording is stricken. Only a policy endorsement can create a notice obligation on the insurer.

- Be aware that sole proprietors have the legal right not to buy workers' compensation coverage for themselves. But this does not mean they are prohibited from pursuing you for workers' compensation benefits--especially when they are clearly under your direction and control.

- Being added as an "additional" insured helps insulate the certificate holder's liability insurance from contractor-generated claims. But remember, it only affords the liability protection that exists in the policy, and additional insured status can be granted only by policy endorsement--not a notation on the certificate.

- There should be no special limitations on an additional insured status. For example, a restriction which ties the additional insured status only to claims arising out of the sole negligence of the contractor does not confer additional insured status at all.

NINE POINTS TO KNOW ABOUT ACCEPTING CERTIFICATES OF INSURANCE

- Unless special policy endorsements apply, aggregate limits shown in a certificate are the total limits available for all losses from all operations of the contractor (or other named insured) during the policy term. That includes any losses from:

  - Other projects of the named insured.
  - All premises rented or owned.
  - Liability coverage contractually provided to other certificate holders.

  The limits and coverage extensions required in your contract provisions can make a difference. Ask for liability limits that apply per project.

- The existence of insurance does not guarantee protection will be available for all contracted services. Two notable areas usually not covered are:

  - Pollution
  - Breach of contract

- Professional liability losses are usually not immediate. Most architect and engineer losses, for example, occur or come to light long after work is completed. Professional liability coverage is virtually always provided on a "claims made" basis. Claims made policies only apply to claims which are made during the policy period. Making sure insurance is in force during the contract does not guarantee insurance will be in force five years later when a building collapses, for example. To be sure insurance is in force for future losses, certificates must be reviewed for years to come. This may be impractical. The most workable protection is to contract with firms having an established reputation.

That's ten points to be aware of, not nine. It's not that we can't count, it's just that we tend to give the extra effort that makes a difference.

If we can provide any further information on certificates, or provide you with certificate review services, contract review or any other type of risk management service, please call or write:

Charles L. Young, Jr., ARM
ARM Tech
23701 Birtcher Drive
Lake Forest, CA 92630-1783
(714) 472-8324

The Additional Insured Book, by Malecki & Gibson, International Risk Management Institute, Inc., Dallas, Texas.

Insuring the Lease Exposure, by Brooks & Malecki, The National Underwriters Company, Cincinnati, Ohio.

Practical Risk Management, by David Warren, Oakland, California.

The Hold Harmless Agreement, by Georgia Chapter of Society of CPCU, The National Underwriter Company, Cincinnati, Ohio.

Construction Risk Management, by Farmer, McIntyre and Gibson, International Risk Management Institute, Inc., Dallas, Texas.

INSURER: County failed to check out second underwriter

FROM 1

article published in The Orange County Register on July 19, which reported the subcontractors' lawsuits.

"We've revised our standards as a result of the article," Walsh said. Nevertheless, she attributed some of the poor oversight to the county Risk Management Department's reliance on a single clerk to perform the required checks on bonding companies.

"We should never have left the process in the hands of one person," Walsh said.

The clerk apparently did not check with the state Department of Insurance. That department's investigatory records indicate that Melchizedek was California Pacific's alleged legal home in September 1992, when Orange County accepted its bond. Inexplicably, the actual bond given the county, however, cited the Turks & Caicos Islands in the British West Indies as California Pacific's legal home.

That's the home of First Assurance, the company that became legally responsible for finishing the firehouse.

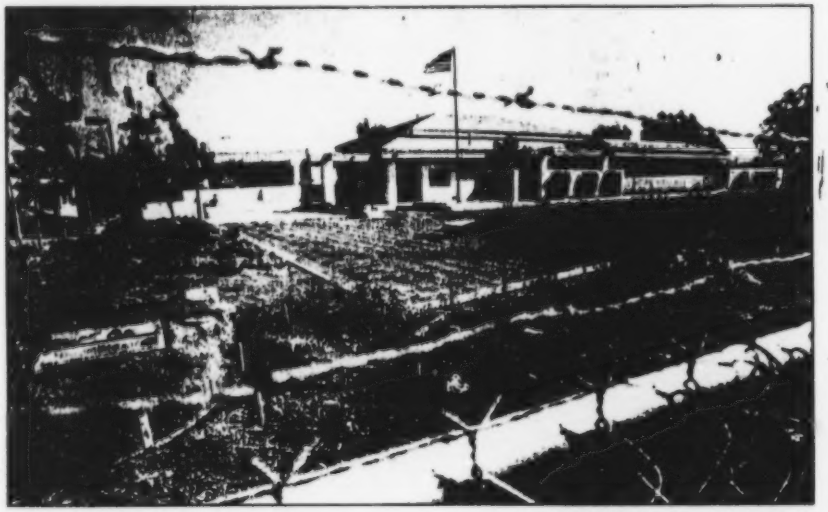
First Assurance, with county approval, bought the $73,000 bond from California Pacific to guarantee payment toplumbing subcontractor Hicks Mechanical Contractors of Orange. The subcontractor had refused to perform further work after posting a legal "stop notice" in Orange County Superior Court, claiming First Assurance owed it $64,000.

The hitch: California Pacific never was a legitimate insurance company.

As with First Assurance, California Pacific did not meet any of the usual standards used to evaluate the insurers who underwrite surety bonds, a kind of insurance that guarantees the payment of a large penalty fee if a contractor fails to finish a job.

Neither First Assurance nor California Pacific was licensed by the state Department of Insurance nor was either on an annual list of federally approved insurers issued by the U.S. Treasury Department.

Although it claimed $469 million in assets on a 1991 financial statement, California Pacific was unable to prove to California regulators that it possessed any net worth. That's why the state Department of Insurance banned it from the state in March.



JEBB HARRIS/The Orange County Register

TROUBLED PROJECT: This fire station sits unfinished amid a snarl of litigation and questionable dealings.

"Absolutely no documentary evidence was submitted in response to the department's request to substantiate any accounting item," a state lawyer wrote California Pacific President Jeff H. Reynolds on March 19. "Not even a bank deposit slip nor even a copy of a stock certificate on an investment was submitted."

Further, the Newport Beach lawyer hired by First Assurance to oversee the fire station construction, Phillip Greer, has asked an Orange County Superior Court judge to allow him to withdraw from representing the company because he hasn't been paid.

According to county records, the county paid Greer and First Assurance $322,678 between Aug. 13 and Oct. 29, 1992.

Plumbing contractor Hicks is outraged.

"I can't believe they took that second bond," he said. "They float around these bonds that nobody can collect on and are no good. I don't have the slightest idea why they don't know how to check them out."

CHRONOLOGY OF A TROUBLED PROJECT: WOODBRIDGE FIRE STATION No. 36

- **Mid-1991:** Orange County signs contract with The Edwards Group, a Tustin contractor, to build a $1 million fire station at 310 East Yale Loop in Irvine.
- **December 1991:** The Edwards Group files for Chapter 13 protection from creditors in U.S. Bankruptcy Court. Coincidentally, the unlicensed insurance company that wrote a completion bond for the project, Winston Hill Assurance Co. Ltd. of the Turks & Caicos islands, also files for bankruptcy in Houston. County officials allow Edwards to buy another completion bond from a second unlicensed Turks & Caicos company, First Assurance & Casualty Co.
- **August 1992:** Edwards becomes insolvent, files for bankruptcy. Orange County supervisors vote to allow the bond insurer, First Assurance, to act as the contractor and finish the construction project.
- **September 1992:** Subcontractors file legal notices with county, complaining they had not been paid for work on the fire station. County allows First Assurance to buy another bond from a foreign insurance company, California Pacific Bankers and Insurance, to cover amount of money in dispute with a subcontractor. California Pacific, at the time, claimed to be legally licensed by a fictitious nation called the Dominion of Melchizedek.
- **March 1993:** State Department of Insurance prohibits California Pacific from doing business in California.
- **April 1993:** Regulators bar First Assurance from operating in California.
- **August 1993:** First Assurance's lawyer asks a judge to relieve him from representing the company because he has not been paid.

Twice burned: Insurance blunder costs O.C., again

GOVERNMENT: Officials' failure to check out a second insurer compounds problems dogging an Irvine firehouse project.

By MARC LIFSHER
The Orange County Register

SACRAMENTO — Orange County officials admit they made a mistake by allowing an unlicensed insurance company to take over management of a $1 million firehouse-construction project from a bankrupt contractor.

Would you believe they made the same mistake twice?

Not only did the county fail to check the credentials of First Assurance Casualty Co. Ltd. of the Turks & Caicos Islands, it failed to check out the bonding company First Assurance used to guarantee payment of firehouse-construction subcontractors.

That bonding company? California Pacific Bankers and Insurance Ltd. The problem? The company at the time claimed to be licensed by the Dominion of Melchizedek, a fictitious nation claimed to exist on the rocky uninhabited Pacific Ocean island of Mapelo, property of Colombia.

The California Department of Insurance subsequently declared both First Assurance and California Pacific insolvent and barred them from doing business in California.

The Irvine fire station isn't finished. Moreover, the county is embroiled in lawsuits filed by some of the 20 subcontractors such as electricians and plumbers who said they had not been paid for their work.

County officials have not been able to explain how they approved the First Assurance and California Pacific bonds. Citing pending litigation, Deputy County Counsel Nicholas Chrisos declined to comment on the case.

Eileen Walsh, the county's director of finance and insurance, said the county only became aware of First Assurance's problems with the state because of an

Please see INSURER Page 6

▶ CHRONOLOGY: Fire station has been troubled project. Page 6

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Contractor's policy excludes cover for additional insured

By MEG FLETCHER

SPRINGFIELD, Ill.—Five years ago, Frederick Claussen was painting at the Glenview Park District indoor ice skating rink when he fell head-first from a 20-foot high scaffold onto a concrete floor.

The accident caused severe brain damage and left the decorating firm employee permanently incapacitated.

Now a negligence lawsuit against the park district by his wife-guardian is severely challenging risk managers' faith in the ability of standard transfer-of-risk agreements to protect building owners from liability when a contractor's employee is injured.

Such agreements require contractors to maintain a commercial general liability policy with minimum limits of coverage and to list the building owner as an additional insured. Contractors typically provide owners with a certificate of insurance containing basic coverage information.

> "... the insurance afforded ... shall not apply to damages arising out of the negligence of the additional insured(s) ..."

Risk managers generally rely on the certificates as proof of the underlying coverage, despite clearly worded disclaimers that the certificates are only informational, attorneys and risk managers agree.

That may soon change. Risk managers likely will become more thorough in their requests for proof of coverage in the wake of the Glenview Park District coverage litigation, which will be heard sometime this spring by the Illinois Supreme Court.

The park district, which relied on the contractor's certificate of insurance, learned only after the accident that the contractor's policy, written by National Union Fire Insurance Co. of Pittsburgh, Pa., contained a non-standard "blanket additional insured endorsement."

Two Illinois courts have ruled that some coverage is eliminated by the endorsement, which excludes "damages arising out of the negligence of the additional insured(s)," though neither court addressed whether the park district was negligent.

The case involves "a complicated contractual issue" that could affect any company that hires contractors and seeks to be named an additional insured under their coverage, warned Robert Enoex, chief counsel for the Illinois Insurance Department.

The department plans to file an amicus brief on behalf of the park district because the endorsement makes the coverage "worthless," he said. In addition, the National Union policy endorsement was never filed with regulators for review, as required under the state's file-and-use system, he added.

The Public Risk Management Assn. may also file an amicus brief.

Following the accident, Mr. Claussen received medical coverage and compensation for lost wages under the workers comp coverage of his employer, National Decorating Service Inc. of Oakbrook, Ill.

Then his wife and legal guardian, Patricia Claussen, filed a lawsuit in Cook County Circuit Court seeking compensatory damages from the park district for negligence, violations of the Illinois Structural Work Act and loss of consortium.

After the suit was filed, the park district was "surprised" to learn that National Union was defending it under a reservations of rights, said Betsy Kutska, executive director of the Park District Risk Management Agency in Lisle, Ill., a self-insurance pool for the Glenview Park District and 109 others in the state.

After researching the case, the park district felt "misled," she said.

The contractor, National Decorating, says that National Union added the "blanket additional insured endorsement" to its CGL policy when the contractor asked to have the Glenview Park District named as an additional insured for the painting project, said attorney Kevin Sido of Hinshaw & Culbertson.

The CGL coverage, which was purchased in August 1987, provided $1 million in both per occurrence and aggregate insurance, as required by the park district.

The park district was also named an additional insured under National Decorating's excess and umbrella liability coverage policy, which provided $2 million in per occurrence and aggregate coverage. That policy was from National Surety Corp. in Chicago, a unit of Fireman's Fund Insurance Co.

A certificate of insurance containing that basic insurance information—but no mention of the endorsement—was forwarded to the park district, which kept it on file.

The circuit court found in 1990 that the primary National Union endorsement did not provide the park district, as an additional insured, with any coverage for damages from its negligence. The court ruled, though, that the National Surety umbrella policy "dropped down" to provide such coverage.

In June 1992, a unanimous, three-judge panel of the Illinois Court of Appeals agreed with the lower court that coverage for an additional insured's negligence was excluded by the endorsement, and also that National Surety must drop down to act as the primary insurer for claims against the park district.

However, the appellate panel found that the endorsement's negligence exclusion did not apply to claims against the park district for alleged violations of the Illinois Structural Work Act.

The unusual law is "an extremely broad and liberal act which protects injured workers," said Robert Chemers, an attorney with Pretzel & Stouffer in Chicago, who is National Union's lead counsel in the case.

"A plaintiff in Illinois would rather go to the jury on a Structural Work Act claim than a common law negligence claim, because the plaintiff's conduct is not an issue," Mr. Chemers noted. Under common law, though, any judgment could be reduced by the plaintiff's own negligence, he explained.

National Union is asking that the state Supreme Court uphold the trial court's finding that the endorsement also precludes coverage for the Structural Work Act claim.

For its part, the Glenview Park District plans to ask the high court to affirm that the endorsement does not exclude claims filed under the Structural Work Act, said Thomas G. DiCiani, an attorney with Ancel, Glink, Diamond & Cope in Chicago, which represents the district. Its filing with the court is due Jan. 20.

And, "It's our position that the negligence exclusion violates public policy because it is so broad that it essentially deprives an insured of any coverage the policy purports to provide," Mr. DiCiani said.

Having the endorsement in force means that the park district is covered only for "rare" cases of "vicarious" liability, such as when an employer is found responsible for its employee's actions, he said.

If the state Supreme Court upholds the endorsement's exclusion of coverage, the park district plans to ask that the case be sent back to the circuit court to determine whether the district was negligent. The district will also ask that National Union be required to continue to defend the park district until such a finding is made.

Several risk managers for major public entities in Illinois were "appalled" when told of the case, Ms. Kutska said. Several plan to check certificates of insurance from contractors in their files to see if National Union is the insurer and, if so, to get copies of underlying policies to see if the blanket endorsement is included, she said.

"I've not seen this type of endorsement," said Bob Esenberg, risk manager for Virginia Beach, Va., and a past president of the Risk & Insurance Management Society Inc.

It's a "very unusual endorsement," agreed Donald S. Malecki, a risk management consultant with D.S. Malecki & Associates Inc. in Cincinnati.

While many insurers have "a preconceived notion" that an additional insured is only protected for vicarious liability, that is not always reflected in their endorsements, said Mr. Malecki, who has written a book on additional insureds.

He warned risk managers that endorsements may become more restrictive in the future.

J. Patrick Gallagher Jr., president of Arthur J. Gallagher & Co. in Itasca, Ill., agreed that this general area of insurance is "typically disputed." Gallagher was National Decorating's broker.

National Union apparently used the controversial endorsement "fairly widely" in Illinois, said Mr. DiCianni, the park district's attorney, basing his comments on a half-dozen telephone calls he has received from other attorneys engaged in litigation over the endorsement.

National Union would not comment. However, in court briefs, the insurer said, "Glenview's conclusion that the insurance bargained for was not intended to be limited to such a slight risk is directed at the wrong party. Glenview's dispute is not with National Union, but NDS."

The park district is also suing National Decorating, charging that the terms of its insurance did not meet the district's requirements.

"Historically, risk managers have accepted certificates of insurance and tucked them away in a file," noted Mr. Chemers, the insurer's attorney. To make sure they are adequately covered, risk managers should obtain a copy of the contractor's endorsement adding them as an additional insured to its CGL policy or, better yet, a copy of the underlying policy, he advised.

However, Ms. Kutska of the self-insurance pool said it would be "extremely burdensome" for a risk manager to obtain a policy each time an entity hired a contractor—an event that occurs thousands of times a year.

To prevent similar disputes in the future, the pool recently revised its insurance specification recommendations to members to outlaw such exclusionary language.

The park district pool's language states that liability coverage should be at least as broad as Insurance Services Office Inc.'s occurrence forms CG 0001 1185, GL 0002 or GL 0404.

The pool also recommends entirely deleting ISO endorsements CG 21 34 11 88 and CG 21 39 11 88, "or other such endorsement or policy provision which limit contractual liability."

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